

P-421/PA-89-828 ADOPTING SETTLEMENT AS MODIFIED AND APPROVING MERGER

BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

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Cynthia A. Kitlinski	Commissioner
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In the Matter of the Proposed Merger of the  
Three U S WEST Operating Companies

ISSUE DATE: October 1, 1990

DOCKET NO. P-421/PA-89-828

ORDER ADOPTING SETTLEMENT AS  
MODIFIED AND APPROVING MERGER

PROCEDURAL HISTORY

On October 2, 1989, Northwestern Bell Telephone Company (Northwestern Bell or the Company) filed notice of its intent to merge into another U S WEST operating company, The Mountain States Telephone and Telegraph Company (MTN). Another U S WEST operating company, Pacific Northwest Bell Telephone Company, would merge into MTN as part of the same merger. The surviving company, renamed U S WEST Communications, Inc. (USWC), would provide local telephone service in 14 states.

The Company stated it did not believe the Commission had jurisdiction over the merger and that it made the filing for informational purposes only.

On October 19, 1989, the Department of Public Service (the Department) made a filing stating it would investigate the proposed merger and report back to the Commission. On April 6, 1990 the Department filed comments stating it believed the proposed merger required Commission approval. Those comments also listed and described certain information the Department considered necessary to determine whether the proposed merger was in the public interest. The Company subsequently supplied much of the information sought by the Department.

On July 10, 1990, the Department filed comments recommending approval of the proposed merger, subject to detailed reporting requirements set forth in those comments. The Company and the Department subsequently reached an agreement on reporting requirements. That agreement was set forth in a stipulation signed and dated August 20, 1990, and filed with the Commission on August 21, 1990.

On August 27, 1990, the Company and the Department filed an amended stipulation, dated August

27, 1990. They asked the Commission to approve and adopt the amended stipulation, which is attached and labelled Attachment A.

The matter came before the Commission on August 28, 1990.

## FINDINGS AND CONCLUSIONS

### **Jurisdiction**

The Commission finds that it has general jurisdiction over the proposed merger under Minn. Stat. §§ 216A.02 (1988) and 237.02 (1988), and specific jurisdiction under Minn. Stat. § 237.23 (1988).

The Commission finds that the proposed merger requires careful examination and will assert jurisdiction. Northwestern Bell provides local exchange service to 73% of Minnesota telephone subscribers; it is currently the designated carrier for intraLATA toll throughout the state. The Commission has a duty to ensure that Company subscribers, toll customers, and interexchange carriers using Company access services, continue to receive high quality service at just and reasonable rates. The Commission will therefore assert jurisdiction over the proposed merger.

### **Overview of the Merger**

Prior to the 1984 Bell System divestiture, Northwestern Bell was a wholly owned subsidiary of AT&T. It is now a wholly owned subsidiary of U S WEST, Inc., one of the seven regional holding companies formed at divestiture. The other two operating companies involved in this merger, Pacific Northwest Bell Telephone Company (PNB) and The Mountain States Telephone and Telegraph Company (MTN), are also wholly owned subsidiaries of U S WEST, Inc.

In 1987 U S WEST, Inc. began to combine, reorganize, and centralize the marketing and network operations of its three operating companies. The Company claims that the merger at issue merely brings the companies' legal structures into conformity with operating realities.

The Company proposes that the merger become effective January 1, 1991.

## **Overview of The Stipulation**

The stipulation submitted by the Department and the Company provides that the proposed merger should be allowed to proceed, subject to detailed and ongoing accounting, reporting, and disclosure requirements. These requirements are intended to ensure prompt and convenient access to the financial and planning information necessary to detect and remedy any negative impact the merger might have on Minnesota ratepayers. The stipulation states that the merger is consistent with the public interest if the accounting, reporting, and disclosure requirements set forth in the stipulation are adopted.

The key provisions of the stipulation may be summarized as follows. The stipulation requires the new company to maintain separate accounts and records for the pre-merger and post-merger long term debt attributable to Northwestern Bell. It requires the new company to compute Minnesota capital structure as a blend or composite of pre-merger and post-merger financing. It requires notification, within 30 days, of any change in long term debt or equity exceeding \$50 million.

The stipulation requires notification and explanation of any change in the new company's cost allocation methodology. It requires notification and explanation if the new company should consolidate its three existing accounting systems into a single system. It requires annual reports, for the next three years, describing the direction of the new company's business, technological developments, service opportunities, and investment levels. It provides the Commission and the Department with comprehensive access to corporate level multi-state financial and planning data.

## **Commission Action**

The Commission concurs with the parties that it appears the primary effect of the merger will be to formalize the operating arrangements under which the Company has been functioning since 1987. There is no evidence that these operating arrangements, or the merger, will have any negative effect on Minnesota ratepayers.

At the same time, however, the accounting, reporting, and disclosure requirements of the stipulation are essential for effective regulation of the new company. Without such safeguards, the financial records and reports of the new company could quickly become a morass from which reliable data could not be obtained. This would prevent the Commission from fulfilling its statutory duty to ensure the provision of adequate service at fair and reasonable rates. Minn. Stat. § 237.06 (1988).

The Commission also believes that two additional items of information are necessary: (1) an annual financial report showing the results of the new company's operations and investments in each of the 14 states in which it will operate and (2) assurance that the new company will give the Commission and the Department access to all documents and data supplied to other state regulatory commissions,

subject to compliance with the terms of any applicable protective orders.<sup>1</sup>

An annual financial report including data for each of the 14 states in which the new company will operate is essential for effective monitoring of the new company's cost allocation and investment decisions. The Commission cannot be sure that Minnesota costs and investments are allocated or committed in a non-discriminatory manner without comparing them to the costs and investments of the other 13 states. Neither can the Commission verify that data offered as Minnesota-specific is accurate or fairly allocated without examining both company-wide data and data specific to other states.

A 14 state financial summary that shows operating data for each of its 14 states will be necessary to monitor the effects of post-merger operating changes. According to the Company, the reorganization after the merger will focus on markets rather than legal entities. The markets will control how the business is managed and money is spent. As a result, costs and revenues will reflect efforts to maximize profits in various markets and ignore jurisdictional boundaries. The reorganization will result in more costs and revenues being allocated among the states. The assignment of costs and revenues will require closer regulatory scrutiny to ensure accurate treatment of the financial data. A larger, more complex 14 state company will require closer regulatory monitoring of the allocations and the formulas used to allocate costs.

Indirect financial amounts are allocated to multiple states using allocation formulas. Allocation formulas use direct costs and revenues along with other measures such as labor hours to apportion indirect amounts. To monitor the changes in operations and allocations, an understanding of the formulas and measures used in the formulas is required.

The 14 state financial summary will provide summary information demonstrating the results of allocations among the states and showing direct cost and revenue information. This report will assist in verifying the allocations and provide a basis to test the reasonableness of the Minnesota jurisdictional amounts as compared to other states. This data along with other information that the Company has agreed to provide will ease the burden of monitoring the post-merger operating changes.

The financial summary report requires that each state's revenues and expenses and capital investments be shown. This schedule will reflect a clearer financial picture by state, permitting a full understanding of the financial data presented. Financial data that only shows some of the data for all 14 states or data for only Minnesota would not allow a complete analysis. Furthermore, since the Company already prepares financial reports by state, it will not be burdensome to provide this report to the Commission.

Similarly, the Department and the Commission may need information filed with other state regulatory commissions to verify or clarify information filed here. Although such information would be subject to disclosure under the Commission's general authority to inspect books and

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<sup>1</sup> If the terms of a protective order conflict with Minnesota law, the new company and the Commission will negotiate a suitable protective order with comparable provisions.

records,<sup>2</sup> it is only reasonable to have clear assurances from the start that such information will be provided promptly. The Commission notes that the Oregon Commission has required such disclosure as a condition for its approval of the proposed merger. This Commission will do so as well.

Apart from the need for the two modifications discussed above, the Commission finds that the stipulation is supported by substantial evidence and is in the public interest. The Commission will therefore accept and adopt the stipulation as modified and will approve the merger, contingent upon the parties' acceptance of the modifications.

Under the terms of the stipulation and under Minn. Stat. § 237.076, subd. 2 (Supp. 1989), the parties have ten days from the date of this Order to reject the modifications. If neither party does so, the Commission's adoption of the stipulation as modified will be final, the merger will be approved, and all requirements contained in the modified stipulation will apply by order of the Commission.

### ORDER

1. The Commission accepts and adopts the stipulation of the parties, dated and filed August 27, 1990, with the modifications set forth below. Adoption of the stipulation as modified is contingent upon the parties' acceptance of the modifications.
  - (a) The new company shall submit an annual financial report showing the results of its operations and investments in each of the 14 states in which it operates. This report shall be presented in the format set forth in Attachment B.
  - (b) On request, the new company shall provide the Commission and the Department copies of or access to all documents and data filed with any other state regulatory commission. This access shall be subject to Commission and Department compliance with the terms of any applicable protective order. If the terms of a protective order conflict with Minnesota law, the new Company and the Commission will negotiate a suitable protective order with comparable provisions.
2. Subject to the parties' acceptance of the modifications set forth above, the merger of Northwestern Bell Telephone Company with the other two U S WEST operating companies is approved. Within ten days of completion of the merger, the surviving company shall notify the Commission that the merger has been completed.

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<sup>2</sup> Minn. Stat. § 216A.05, subd. 3 (1) (1988) grants the Commission broad powers to compel the production of documents "kept by any regulated business within or without the state," emphasis added. Similarly, Minn. Stat. § 237.11 (1988) grants the Commission comprehensive rights to inspect books, records, and documents of "every telephone company subject to the provisions of this chapter, wherever organized, . . ." emphasis added.

3. The parties have ten days from the date of this Order to reject the modifications set forth above. If neither party does so, the merger is approved and the terms of the stipulation, including the modifications set forth above, constitute the final Order of the Commission.
4. This Order shall become effective immediately.

BY ORDER OF THE COMMISSION

Richard R. Lancaster  
Executive Secretary

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